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TAGS: ECON EFIN EINV CH
SUBJECT: HAITONG'S BACKDOOR LAUNCH INTO THE MARKET

REF: A. SHANGHAI 334

¶B. SHANGHAI 478

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¶1. (SBU) Summary: Haitong Securities became the first securities company to list via a backdoor listing in China, on July 31, after it completed a reverse takeover of Shanghai Urban Agro-Business. It was forced to use a backdoor listing since, on its own, it did not meet Chinese listing requirements. Other securities firms are in the pipeline to follow Haitong onto the market through backdoor listing as they hope to raise funds necessary to make them competitive with the inevitable entry of more competitive international firms. End Summary.

¶2. (SBU) Econoff and Economic Assistant attended the Haitong Securities Company's listing ceremony on the floor of the Shanghai Stock Exchange on July 31. Haitong is the third securities firm to list in China and the first to do so via a backdoor listing. (Note: Hong Yuan Securities listed in 1994; Citic Securities Co., one of the country's biggest brokerage firms, listed in 2002.) On Haitong's first day of trading, it declined 6.7 percent from its initial price of 56.01 to 51.65. (Note: See Ref A for a report on Finatt's meeting with Haitong Securities on May 16).

¶3. (SBU) At the listing ceremony, Haitong Securities Company International Business Department General Manager Liao Rongyao and Haitong Securities Director Wu Bin said Haitong intended to use the money it raised on the capital markets to expand its business. It hoped to acquire several smaller securities companies and develop its stock index futures portfolio (Ref B). Wu also said that being a listed company would enhance Haitong's corporate image and increase public awareness of the

company.

Mechanics of the Backdoor Listing

¶4. (SBU) Z-Ben Advisors Principal Peter Alexander, in a separate meeting on July 28, told Econoff that Haitong effected its backdoor listing by purchasing Shanghai Urban Agro-Business Limited. Shanghai Urban was a listed company owned by Shanghai Municipal government's Bright Foods Group. To effect the transaction, Shanghai Urban transferred all of its assets and liabilities, including retired employees, back to its parent in exchange for 756 million RMB (USD 100 million). Before this backdoor listing was announced on October 16, 2006, Shanghai Urban's stock was worth 6.38. Following the announcement of Haitong's intended reverse takeover, trading of Shanghai Urban's stock was suspended until January 5 when it reopened at 6.38 RMB per share. It had risen to 56 RMB per share as of July 31, on investor's anticipation of the takeover.

¶5. (SBU) Haitong's Wu told Econoff that the procedures and regulations governing controlling backdoor listings were "not very clear and very complicated." He noted that Haitong had been forced to deal with many different regulators at the same time as they attempted to discern what information was required and how Haitong should proceed.

¶6. (SBU) Haitong, opened in 1988, was one of three securities companies owned by the Shanghai Municipal government. Shanghai also owns the Shenyin Wanguo and Guotai Junan securities firms. According to Wu, Haitong had initially been owned by the Ministry of Finance and was transferred several years ago from the Ministry of Finance to the Shanghai government.

¶7. (SBU) Haitong's Liao said that Haitong had initially targeted

a Shenzhen-listed company called the Liulu Industrial Company. (Note: Liulu is a company under the direction of PetroChina that has yet to undergo share reform. End note.) Liao said that the Shanghai government had objected to Haitong's "moving out of town" and provided a list of six ailing Shanghai Government-owned listed companies for Haitong's "consideration." One of these was Shanghai Urban.

Back(door Listing) to the Future?

¶8. (SBU) Z-Ben Advisors Alexander noted that several other Chinese brokerage firms, such as China Merchants Securities Co. and Guotai Junan Securities Co. are also preparing to launch initial public offerings via backdoor listings. Many of these companies have already started the process of purchasing listed shell companies. Backdoor listings provide the only method for Chinese securities firms to list due to the Chinese Securities Regulatory Commission's listing-requirement that companies have three years of profitability. Securities firms, who up until 18 months ago had suffered through China's five bear market, did not meet this qualification. According to Alexander, Chinese securities firms were hoping to go public as soon as possible so that they could raise funds to prepare themselves for what many see as the inevitable entry of more competitive foreign securities firms.

Comment

¶9. (SBU) Attending the ceremony and providing official blessing was Shanghai Vice Mayor Yang Dinghua. In her remarks, she said that Haitong's listing was another step towards insuring Shanghai's place as an international financial center. Shanghai's interference in helping Haitong "select" a Shanghai-owned and -listed company demonstrates the lengths to

which municipal governments will go to protect and promote its own during mergers and acquisitions. Shanghai Stock Exchange Executive Vice President referred to Shanghai's stock exchange as "The Shanghai Financial Stock Exchange" on July 27 (Ref B) because financial services companies account for 80 percent of the value on the market. Indeed, Shanghai's reputation as an international financial capital and the success of the Shanghai stock market appear to be increasingly interlinked.
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